Dr Klaus D Wiegel, VIC

15 November 2003

Productivity Commission
Inquiry into First Home Ownership
By e-mail

Dear Sir,

Submission to Inquiry into First Home Ownership

I would like to make a submission for your consideration, knowing that it addresses only some minor aspects of the complex topic.

From the Issues Paper it appears to me that the purchase of first homes is now back to the long-term range of between 100,000 to 120,000 purchases per annum, after the First-Home-Owners-Grant induced spike between 2000 and 2002. Therefore, should the Government(s) really worry about this 'retreat back to normal'?

As a market economist, I believe that apart from other major factors (like the supply of sufficient land to build new dwellings) tax incentives and disincentives are playing a major part in distorting the First Home Owners market. Let me elaborate just on three of them:

1) First Home Owner Grant (FHOG)

   From a naïve, external observer's point of view, it appears strange that the FHOG is accessible to babies and toddlers, to people who haven't bought a 'first home' in 60, 70 or 80 years and now like to use this tax incentive to do so or to first home owners who buy million-dollar properties.
   If this market distorting tax incentive, paid for by the average Australian tax payer to subsidise first home owners into their first property, is necessary at all, it should be limited by age of the applicant, say 18 to 81 years and limited to the average medium dwelling purchase price. My reasoning is that first home owners who can afford above average dwelling purchases don't need to be subsidised by the average Australian into it.

   By limiting (or even eliminating) the FHOG, a lot of demand would fall away and housing prices might reduce their steep increases.

2) Stamp Duties

   Stamp Duties, especially those as high as on property purchases, make the property transactions very costly and economically less efficient.

I submit to review this part of the taxation system with a view to eliminating Stamp Duties on property transactions and increase property tax to compensate for it.
This would reduce the price of first homes and at the same time increase the supply of homes from existing property owners as they would prefer to sell their oversized, (tax) costly properties and move to smaller, less costly ones.
This proposal would also transfer the property tax burden from average transactors (and tax payers) to primarily wealthy property owners and to a lot of investors who otherwise pay little tax in Australia.
This increased property tax could be along the same 'social policy' lines as the existing, much lower tax already is: Have exemptions for low property values (which again will benefit the majority of first home owners), and have a progressively rising percentage for higher property values.

3) Capital Gains Tax (CGT)

Another major tax distortion is the current CGT exemption of the private residence. It is the last major resort for investors to avoid legally CGT and many people pouring all their assets into this unproductive home ownership. However, the last few years have proven them absolutely right to do so!

To partly reduce this distortion, a CGT should also be levied on private residences, even if it is only 50% of the currently applicable CGT. It would make investments in unproductive dwellings more comparable to investments in productive assets and should reduce the tax-distorted demand for housing and cool off housing price increase.
This will result in lower increases of dwelling prices and will make First Home Ownership more affordable.

Yours truly,

Klaus Wiegel